

DISTRICT OF COLUMBIA
DEPARTMENT OF INSURANCE AND SECURITIES REGULATIONNOTICE OF FINAL RULEMAKING

The Commissioner of Insurance and Securities Regulation, pursuant to the authority set forth in section 23 of the District of Columbia Health Maintenance Organization Act of 1996 (the "Act"), effective April 9, 1997, D.C. Law 11-235, D.C. Code § 35-4522 (1997), hereby gives notice of the adoption of the following amendment to Title 26 of the District of Columbia Municipal Regulations (DCMR) (Insurance). The amendment adds a new Chapter 31 to establish requirements and guidelines for the investment of the funds of a Health Maintenance Organization as required under section 12 of the Act, D.C. Code § 35-4511. Several technical changes have been made to the text of the proposed rulemaking as published at 46 DCR 4202 (May 7, 1999). These rules will become effective upon the publication of this notice in the D.C. Register.

Title 26 DCMR (Insurance) is amended by adding a new Chapter 31 to read as follows:

Chapter 31 INVESTMENT GUIDELINES FOR HEALTH MAINTENANCE
ORGANIZATIONS (HMOs)

3101 GENERAL REQUIREMENTS AND LIMITATIONS

- 3101.1 An HMO may invest its funds only as provided under this Chapter. Notwithstanding the provisions of these regulations, the Commissioner may, after notice and opportunity for a hearing, order an HMO to limit or withdraw from certain investments, or discontinue certain investment practices, to the extent the Commissioner finds that such investments or investment practices are hazardous to the financial condition of the HMO.
- 3101.2 No investment or loan, shall be made or engaged in by an HMO unless the investment or loan has been authorized by the board of directors, or by a committee thereof charged with the duty of supervising investments and loans. Nothing contained in this Chapter shall prevent the board of directors of an HMO from depositing any of its securities with:
- (a) A committee appointed for the purpose of protecting the interest of security holders; or
 - (b) The authorities of any state or the District where it is necessary to do so in order to secure permission to transact business therein.
- 3101.3 Nothing contained in this Chapter shall prevent the board of directors of an HMO from depositing any securities as

JUL 16 1999

collateral for the securing of any bond required for the business of the HMO.

3101.4 An HMO shall not pay any commission or brokerage fee for the purchase or sale of property whether real or personal, in excess of an amount that is usual and customary in the locality where such purchases or sales are made, and the HMO shall maintain information regarding payments of commissions and brokerage fees shall be maintained for at least three (3) years.

3101.5 No HMO shall knowingly invest in or make a loan secured by any property, directly or indirectly, whether real or personal, in which any officer or director of such HMO has a financial interest, nor shall an HMO make a loan of any kind to any officer or director of such HMO, except that this subsection shall not apply in circumstances where the financial interest of such officer or director, if any, is so remote as to not give rise to a conflict of interest. Notwithstanding the provisions of this subsection, the Commissioner may approve a transaction between an HMO and its officers or directors under this section if he or she is satisfied that:

- (a) The transaction is entered into in good faith for the advantage and benefit of the company;
- (b) The amount of the proposed investment or loan does not violate any other provision of this Chapter, and the loan does not exceed the fair market normal value of the property securing the loan, or the amount of the investment does not exceed the interest which the HMO proposes to acquire, and the transaction is otherwise fair and reasonable; and
- (c) The transaction will not adversely affect the liquidity of the HMO's investments, its ability to comply with requirements of this Chapter, or the payment of its claims and obligations.

3102 VALUATION OF INVESTMENTS

3102.1 In applying the percentage limitations imposed by this Chapter, there shall be used as a base the total of all assets which would be admitted by this Chapter without regard to percentage limitations. All legal measurements used as a base in the determination of all qualified investments shall consist of the amounts determined at the most recent year end as adjusted for the subsequent acquisition and disposition of such investments.

3102.2 Investments shall be valued in accordance with the published valuation standards of the National Association of Insurance Commissioners (NAIC). Investments in

JUL 16 1999

securities for which the NAIC has not published valuation standards in its Valuations of Securities manual, or its successor publication, shall be valued as set forth in subsections 3102.3 through 3102.7.

3102.3 All obligations having a fixed term and rate shall, if not in default as to principal or interest, be valued as follows:

(a) If purchased at par, at the par value; or

(b) If purchased above or below par, on the basis of the purchase price adjusted so as to bring the value to par at maturity and so as to yield in the meantime the effective rate of interest at which the purchase was made.

3102.4 Common, preferred or guaranteed stocks shall be valued at market value.

3102.5 Other security investments shall be valued at market value.

3102.6 Other investments, including real property, shall not be valued at more than the purchase price. The purchase price for real property includes capitalized permanent improvements, less depreciation spread evenly over the life of the property or, at the option of the company, less depreciation computed on any basis permitted under section 301 of the Internal Revenue Code, 26 U.S.C. § 301 et seq., and regulations adopted thereunder. Such investments that have been affected by permanent declines in value shall be valued at not more than market value.

3102.7 Any investment, including real property, not purchased by an HMO but acquired in satisfaction of a debt or otherwise shall be valued in accordance with the applicable procedures for that type of investment contained in this Chapter. For purposes of applying the valuation procedures in the case of any investment acquired in satisfaction of debt, the purchase price shall be deemed to be the market value at the time the investment is acquired or the amount of the debt (including interest, taxes and expenses), whichever amount is less.

3103 AUTHORIZED INVESTMENTS

3103.1 Any HMO may acquire the assets set forth in subsections 3103.2 through 3103.18, inclusive. Any restriction, exclusion or provision appearing in any subsection shall apply only with respect to the authorization of the particular subsection in which it appears and shall not constitute a general prohibition and shall not be applicable to any other subsection. The qualifications

JUL 16 1999

or disqualifications of an investment under one subsection shall not prevent its qualification in whole or in part under another subsection, and an investment authorized by more than one subsection may be held under whichever authorizing subsection the HMO elects. An investment which qualified under any subsection at the time it was acquired or entered into by an HMO shall continue to be qualified under that subsection. An investment in whole or in part may be transferred from time to time, at the election of the HMO, to the authority of any subsection under which it qualifies, whether originally qualifying thereunder or not.

3103.2 Direct obligations of the United States for the payment of money, or obligations for the payment of money, to the extent guaranteed or insured as to the payment of principal and interest by the United States.

3103.3 Direct obligations for the payment of money, issued by an agency or instrumentality of the United States, or obligations for the payment of money to the extent guaranteed or insured as to the payment of principal and interest by an agency or instrumentality of the United States.

3103.4 Direct, general obligations of the District or any state of the United States for the payment of money, or obligations for the payment of money to the extent guaranteed or insured as to the payment of principal and interest by the District or any state of the United States, on the following conditions:

- (a) The state or the District has the power to levy taxes for the prompt payment of the principal and interest of such obligations; and
- (b) The state or the District shall not be in default in the payment of principal or interest on any of its direct, guaranteed or insured general obligations at the date of such investment.

3103.5 Direct, general obligations of any political subdivision of any state of the United States for the payment of money, or obligations for the payment of money to the extent guaranteed as to the payment of principal and interest by any political subdivision of any state of the United States, on the following conditions:

- (a) The obligations are payable or guaranteed from ad valorem taxes;
- (b) Such political subdivision is not in default in the payment of principal or interest on any of its direct or guaranteed obligations;

JUL 16 1999

- (c) No investment shall be made under this section in obligations which are secured only by special assessments for local improvements; and
- (d) An HMO shall not invest under this section more than two percent (2%) of its admitted assets in obligations issued or guaranteed by any one such political subdivision.

3103.6

Anticipation obligations of any political subdivision of any state of the United States, including but not limited to bond anticipation notes, tax anticipation notes, preliminary loan anticipation notes, revenue anticipation notes and construction anticipation notes, for the payment of money within twelve (12) months from the issuance of the obligation on the following conditions:

- (a) Such anticipation notes must be a direct obligation of the issuer under the conditions set forth in subsection 3103.5.
- (b) Such political subdivision is not in default in the payment of the principal or interest on any of its direct general obligations or any obligation guaranteed by such political subdivision;
- (c) The anticipated funds must be specifically pledged to secure the obligations; and
- (d) An HMO shall not invest under this subsection more than two percent (2%) of its admitted assets in the anticipation obligations issued by any one such political subdivision.

3103.7

Obligations of any state of the United States, a political subdivision thereof, or a public instrumentality of any one or more of the foregoing, for the payment of money, on the following conditions:

- (a) The obligations are payable from revenues or earnings of a public utility of such state, political subdivision, or public instrumentality which are specifically pledged therefor;
- (b) The law under which the obligations are issued requires rates for service to be charged and collected at all times such that they will produce sufficient revenues, in addition to the revenues needed to pay all operating and maintenance charges of the public utility, to pay all principal and interest on such obligations;
- (c) No prior or parity obligations payable from the revenues or earnings of that public utility are in

JUL 16 1999

default at the date of such investment;

- (d) An HMO shall not invest more than twenty percent (20%) of its admitted assets under this section; and
- (e) An HMO shall not invest under this section more than two percent (2%) of its admitted assets in the revenue obligations issued in connection with any one facility.

3103.8

Obligations of any state of the United States, a political subdivision thereof, or a public instrumentality of any one or more of the foregoing, for the payment of money, on the following conditions:

- (a) The obligations are payable from revenues or earnings, excluding revenues or earnings from public utilities, specifically pledged therefor by such state, political subdivision, or public instrumentality;
- (b) No prior or parity obligation of the same issuer payable from revenues or earnings from the same source has been in default as to principal or interest during the five (5) years preceding the date of such investment, but such issuer need not have been in existence for that period, and obligations acquired under this section may be newly issued;
- (c) An HMO shall not invest in excess of twenty percent (20%) of its admitted assets under this subsection;
- (d) An HMO shall not invest under this section more than two percent (2%) of its admitted assets in the revenue obligations issued in connection with any one facility; and
- (e) An HMO shall not invest under this section more than two percent (2%) of its admitted assets in revenue obligations payable from revenue or earning sources which are the contractual responsibility of any one single credit risk.

3103.9

Direct, unconditional obligations of a solvent business corporation for the payment of money, including obligations to pay rent for equipment used in this business on the following conditions:

- (a) The corporation shall be incorporated under the laws of the District, the United States or any state thereof;

JUL 16 1999

- (b) If such stocks have been outstanding prior to purchase, an HMO shall not invest under this subsection in such stock if prescribed current or cumulative dividends are in arrears;
- (c) An HMO shall not invest more than thirty-three and one-third percent ($33 \frac{1}{3}\%$) of its admitted assets under this subsection and an HMO shall not invest more than fifteen percent (15%) of its admitted assets under this subsection in stocks which, at the time of purchase, are not sinking fund stocks. An issue of preferred or guaranteed stock shall be a sinking fund stock when:
 - (1) such issue is subject to a one hundred percent (100%) mandatory sinking fund or similar arrangement which will provide for the redemption of the entire issue over a period not longer than forty (40) years from the date of purchase;
 - (2) annual mandatory sinking fund installments on each issue commence not more than ten (10) years from the date of issue; and
 - (3) each annual sinking fund installment provides for the purchase or redemption of at least two and one-half percent ($2 \frac{1}{2}\%$) of the original number of shares of such issue; and
- (d) An HMO shall not invest under this subsection more than two percent (2%) of its admitted assets in the preferred or guaranteed stocks of any one such corporation.

3103.13 Common stock issued by any solvent business corporation incorporated under the laws of the District, the United States or any state thereof, on the following conditions:

- (a) The issuing corporation must have tangible net worth of \$1,000,000 or more;
- (b) An HMO may not invest more than an amount equal to its net worth under this section;
- (c) An HMO may not invest under this subsection an amount equal to more than ten percent (10%) of its net worth in the common stock of any one corporation;

3103.14 Shares of common stock or units of beneficial interest issued by a solvent business corporation or trust incorporated or organized under the laws of the District, the United States or any state thereof, on the following

JUL 16 1999

conditions:

- (a) If the issuing corporation or trust is advised by an investment advisor which is the HMO or an affiliate of the HMO, the issuing corporation or trust shall have net assets of \$100,000 or more, or if the corporation or trust has an unaffiliated investment advisor, the issuing corporation or trust shall have net assets of \$10,000,000 or more;
- (b) The issuing corporation or trust is registered as an investment company with the Securities and Exchange Commission pursuant to the Investment Company Act of 1940, as amended, 15 U.S.C. §§ 80a-1 et seq.;
- (c) An HMO shall not invest under this subsection more than the greater of \$100,000 or ten percent (10%) of its admitted assets in any one bond fund, municipal bond fund, or money market fund;
- (d) An HMO shall not invest under this subsection more than ten percent (10%) of its net worth in any one common stock fund, balanced fund, or income fund;
- (e) An HMO shall not invest more than fifty percent (50%) of its admitted assets in bond funds, municipal bond funds, and money market funds under this subsection; and
- (f) An HMO's investments in common stock funds, balanced funds or income funds when combined with its investments in common stocks made under subsection 3103.13 shall not exceed the aggregate limitation provided by subsection 3103.13(b).

3103.15 Shares of, or accounts or deposits with, savings and loan associations or building and loan associations, on the following conditions:

- (a) The shares, accounts, or deposits, or investments in any form legally issuable shall be of a withdrawable type and issued by an association which has the insurance protection afforded by the Federal Savings and Loan Insurance Corporation. Nonwithdrawable accounts which are not eligible for insurance by the Federal Savings and Loan Insurance Corporation shall not be eligible for investment under this subsection;
- (b) The association shall have tangible net worth of not less than \$1,000,000;
- (c) The investment shall be in the name of and owned by

JUL 16 1999

the HMO, unless the account is under a trusteeship with the HMO named as the beneficiary;

- (d) An HMO shall not invest more than fifty percent (50%) of its admitted assets under this subsection; and
- (e) Under this subsection, an HMO shall not invest in any one such association an amount in excess of two percent (2%) of its admitted assets or an amount which is fully insured by the Federal Savings and Loan Insurance Corporation, whichever is greater.

3103.16 Direct, unconditional obligations for the payment of money secured by the pledge of any investment which is authorized by any of the preceding subsections, on the following conditions:

- (a) The investment pledged shall by its terms be legally assignable and shall be validly assigned to the HMO;
- (b) The investment pledged shall have a fair market value which is at least twenty-five percent (25%) greater than the amount invested under this subsection, except that a loan may be made up to 100% of the full fair market value of the collateral that would qualify as an investment under subsection 3103.2 provided it qualifies under paragraph (a) of this subsection; and
- (c) An HMO's investment under this subsection when added to its investment of the category of the collateral pledged shall not cause the sum to exceed the limits provided by the subsection authorizing that category of investments.

3103.17 Real estate (including leasehold estates and leasehold improvements) for the convenient accommodation of the HMO's business operations, including home office, branch office, medical facilities and field office operations, on the following conditions:

- (a) Any parcel of real estate acquired under this subsection may include excess space for rent to others, if it is reasonably anticipated that such excess will be required by the HMO for expansion or if the excess is reasonably required in order to have one or more buildings that will function as an economic unit; and
- (b) Such real estate may be subject to a mortgage.

3103.18 Investments of any kind, in the complete discretion of

JUL 16 1999

the HMO, without regard to any condition of, restriction in, or exclusion from subsections 3103.2 through 3103.17, inclusive, and regardless of whether the same or a similar type of investment has been included in or omitted from any such subsection; provided that an HMO shall not invest under this subsection more than the lesser of: (1) ten percent (10%) of its admitted assets; or (2) 50% of the amount by which its net worth exceeds the minimum requirements of a new HMO to qualify for a certificate of authority.

3199 DEFINITIONS

3199.1 "Admitted asset" means the investments authorized or permitted under this chapter, and in addition, includes only the following:

- (a) Petty cash and other cash funds in the HMO's principal or official branch office(s) and under the control of the HMO;
- (b) Immediately withdrawable funds on deposit in demand accounts, in a bank, savings bank, or trust company as defined in subsection 3199.4, or like funds actually in the principal or any official branch office at statement date, and in transit to such bank, savings bank or trust company with authentic deposit credit given prior to the close of business on the fifth (5th) bank working day following the statement date;
- (c) The amount fairly estimated as recoverable on cash deposited in a closed bank, savings bank, or trust company, if qualifying under subsection 3199.4 prior to the suspension of such bank, savings bank or trust company;
- (d) Bills and accounts receivable collateralized by securities of the kind in which the HMO is authorized to invest;
- (e) Premiums receivable from: (1) groups or individuals which are not more than sixty (60) days past due; and (2) the District, the United States, any state of the United States or any political subdivision thereof which is not more than ninety (90) days past due;
- (f) Amounts due under insurance policies or reinsurance arrangements from insurance companies authorized to do business in the District;
- (g) Tax refunds due from the District, the United States, any state of the United States or any

JUL 16 1999

percent (10%) of the organization's admitted assets or twenty-five percent (25%) of the HMO's net worth as defined in this chapter. Any amount outstanding more than three (3) months shall be deemed not current. For purpose of this paragraph "affiliates" shall have the same meaning as that term is defined in D.C. Code § 35-3701;

- (r) Intangible assets, including, but not limited to, organization good will and purchased good will, to the extent reported in the most recent annual or quarterly financial statement filed with the Commissioner after April 9, 1997. However, such assets shall be amortized, by the straight-line method, to a value of zero no later than December 31, 1999; provided, however, that no HMO shall be required pursuant to the foregoing provision to amortize such assets in an amount greater than \$300,000 in any one year, and in cases where amortization of such assets by December 31, 1999 would otherwise require amortization of an annual amount in excess of \$300,000, the HMO shall be required only to amortize such assets at a rate of \$300,000 per year until all such assets have been amortized to a value of zero, unless the continuation of the current amortization schedule would result in an earlier zero value, in which case the current amortization schedule shall be applied;
- (s) Amounts due from patients or enrollees for health care services rendered which are not more than sixty (60) days past due;
- (t) Amounts advanced to providers under contract to the organization for services to be rendered to enrollees pursuant to the contract. Amounts advanced must be for a period of not more than three (3) months and must be based on historical or estimated utilization patterns with the provider and must be reconciled against actual incurred claims at least semi-annually. Amounts due in the aggregate may not exceed fifty percent (50%) of the organization's net worth as defined in subsection 3199.13. Amounts due from a single provider may not exceed the lesser of five percent (5%) of the HMO's admitted assets or ten percent (10%) of the HMO's net worth;
- (u) Cost reimbursement due from the Health Care Financing Administration of the U.S. Department of Health and Human Services, for furnishing covered medicare services to medicare enrollees which are not more than twelve (12) months past due; and

DISTRICT OF COLUMBIA REGISTER

JUL 16 1999

- (v) Prepaid rent or lease payments no greater than three (3) months in advance, on real property used for the administration of the HMO's business or for the delivery of medical care.
- 3199.2 "Business corporation" means a corporation organized for other than not-for-profit purposes.
- 3199.3 "Business entity" means a sole proprietorship, a corporation, an association, a partnership, a limited partnership, a business trust, or a limited liability company.
- 3199.4 "Bank, savings bank or trust company" means any bank, savings bank or trust company organized and supervised under the laws of the District, the United States or any state thereof, if the bank, savings bank or trust company has the insurance protection afforded by an agency of the United States.
- 3199.5 "Capital" means capital stock paid up, if any, and its use in a provision does not imply that a not for profit HMO without stated capital stock is excluded from the provision. The capital of such an HMO will be zero.
- 3199.6 "Direct" when used in connection with "obligation" means that the designated obligor shall be primarily liable on the instrument representing the obligation.
- 3199.7 "District" means the District of Columbia.
- 3199.8 "Facility" means and includes real estate and any and all forms of tangible personal property and services used constituting an operating unit.
- 3199.9 "Guaranteed or insured" means that the guarantor or insurer will perform or insure the obligation of the obligator or will purchase the obligation to the extent of the guaranty or insurance.
- 3199.10 "Mortgage" shall include a trust deed or other lien on real property securing an obligation for the payment of money.
- 3199.11 "Servicer" means a business entity that has a contractual obligation to service a pool of mortgage loans. The service provided shall include, but is not limited to, collection of principal and interest, keeping the accounts current, maintaining or confirming in force hazard insurance and tax status and providing supportive accounting services.
- 3199.12 "Single credit risk" means the direct, guaranteed or insured obligations of any one business entity including

JUL 16 1999

affiliates thereof.

3199.13 "Surplus" means the amount properly shown as total net worth on a company's balance sheet, plus all voluntary reserves, but not including capital paid-up.

3199.14 "Tangible net worth" means the par value of all issued and outstanding capital stock of a corporation (or in the case of shares having no par value, the stated value) and the amounts of all surplus accounts less the sum of:

- (a) Such intangible assets as deferred charges, organization and development expense, discount and expense incurred in securing capital, good will, trademarks, trade names and patents;
- (b) Leasehold improvements; and
- (c) Any reserves carried by the corporation and not otherwise deducted from assets.

3199.15 "Unconditional" when used in connection with the term "obligation" means that nothing remains to be done or to occur to make the designated obligor liable on the instrument, and that the legal holder shall have the status at least equal to that of general creditor of the obligor.